Directorate of
Intelligence

~~Secret~~

25X1

Japanese Overseas Direct Investments: Recent Trends and Future Prospects

25X1

A Research Paper

~~Secret~~

EA 83-10112
June 1983

Copy 288

Page Denied

Sanitized Copy Approved for Release 2011/02/07 : CIA-RDP84S00553R000200170002-8

Directorate of Intelligence

Secret [redacted]

25X1

Japanese Overseas Direct Investments: Recent Trends and Future Prospects [redacted]

25X1

A Research Paper

This paper was prepared by [redacted] Office of East Asian Analysis. It was coordinated with the National Intelligence Council. [redacted]

25X1

25X1

Comments and queries are welcome and may be directed to the Chief, Japan Branch, OEA, on [redacted]

25X1

Secret
EA 83-10112
June 1983

25X1

Japanese Overseas Direct Investments: Recent Trends and Future Prospects

25X1

Key Judgments

Information available as of 13 June 1983 was used in this report.

Japan moved rapidly in the 1970s to increase investments in foreign countries in response to strong protectionist pressures from abroad and shifting market competitiveness at home. We believe that this move will ease some of Japan's current trade problems. Japan now accounts for more than 5 percent of the world's total overseas direct investment, a figure that will rise to 10 percent by 1990 if the current trend continues. Japanese firms overseas employ about 700,000 people. We expect that number will more than double by 1990 as Japanese businesses continue to ship out capital because of limited investment opportunities at home, high demand for Japanese products overseas, and protectionist measures against Japanese exports. 25X1

Japanese investment is moving away from the earlier emphasis on resource exploitation and is focusing more on manufacturing industries. Simultaneously, the geographical emphasis has shifted to the United States and Western Europe and away from developing countries. A select number of stable LDCs, such as the ASEAN countries, however, will continue to receive a significant share of manufacturing investments. 25X1

The Japanese Government offers a variety of incentives and special programs to help firms, including small businesses, invest offshore, such as risk insurance, modest tax breaks, counseling, and information services. Government financial institutions provide only a small amount of the cash needed to finance overseas operations but are able to aim their limited funds at selected countries or particular investment sectors. In the 1970s, for example, Tokyo encouraged resource development investments to ensure access to raw materials. The government has shifted its emphasis toward manufacturing investments in advanced countries such as the United States and in Western Europe, where trade frictions are growing and has made Export-Import Bank funds available for this purpose. Despite Tokyo's endorsement of capital exports, Japanese industry and labor are beginning to worry about the long-range effect that rapid expansion of production facilities abroad will have on domestic employment. 25X1

25X1

The United States will benefit most from current trends. We estimate that for every $1 billion in new investment at least 5,000 new jobs would be created in the United States. In the next few years, the capital-intensive transportation industry should lead the list of Japanese investments, as automobile firms attempt to overcome trade barriers and parts suppliers move to service the growing fleet of Japanese cars in the United States. In terms of the number of investments, the electronics industry and other firms manufacturing high-technology products should play a larger role as companies continue to open or expand local production facilities and seek links with US firms. 25X1

Contents

25X1

Japanese Overseas Direct Investments: Recent Trends and Future Prospects

25X1

The cumulative total of Japan's direct overseas investments from 1951 to the end of Japan's FY 1982 reached $53.1 billion, according to the Ministry of Finance.[1] Japan is fourth after the United States, Great Britain, and West Germany in the world and accounts for roughly 5.3 percent of direct investments worldwide. The small size of Japan's share reflects its late start—almost all of Japanese outlays have occurred since 1969 when Tokyo began easing restrictions on investments. Japanese companies now operate in 120 countries and have more than 7,000 affiliates.

Japanese subsidiaries overseas employ over 700,000 local workers, more than 80 percent of whom are in manufacturing industries. About 60 percent of the workers are employed in affiliates in Asia, mostly in textile and electrical equipment plants; over 11 percent are in manufacturing plants in advanced countries.

The Pattern of Growth

Japanese firms have invested overseas in order to offset limited expansion opportunities or higher costs at home and to gain access to new sources of raw materials and new markets. Overseas investments, as a result, went from nearly zero in the late 1960s to $10.3 billion by early 1974 and accelerated even more rapidly after the mid-decade recession.

[1] Japan's fiscal year begins on 1 April of the stated year. The $53.1 billion represents direct investment approvals and not book values of existing overseas investments. Ministry of Finance data on Japan's direct investments overseas are compiled per fiscal year on the basis of licenses granted or reports received. Official tabulations do not show the exact amount of the actual investment, withdrawals, or reinvestments of earnings. Such official statistics are inflated from the book value of investments abroad. The Bank of Japan compiles investment figures on the basis of balance of payments. These statistics do not show reinvested earnings, nor are they broken down by type of industry or region. Whereas the Finance Ministry reports an aggregate of $45.5 billion in overseas direct investments as the end of fiscal year 1981, for example, the Bank of Japan records $24.5 billion, about half that amount, as the cumulative total at the beginning of calendar year 1982. For this paper we use the Ministry of Finance listings, unless otherwise noted. This study is based largely on official Japanese sources.

The investments that dominated the early 1970s were:
- Raw material development projects in resource-rich countries.
- Assembly plants for labor-intensive products, mainly in Southeast Asian countries.
- Commercial and financial offices in industrialized countries.

25X1

Between 1972 and 1977 Japan's direct investments overseas were almost evenly divided among commerce and service industries (37 percent), manufacturing industries (35.1 percent), and resource development industries (28.3 percent). In the next two years, however, manufacturing and commerce and service industries accounted for nearly 85 percent of new outlays as Japanese firms moved to offset the impact of fluctuating exchange rates and trade barriers. Geographically, this was reflected in a shift toward the United States and other industrial countries and away from Latin America and other developing regions (see figure 1). Asia, nonetheless, continued to receive a large proportion of investments each year, reflecting its position as both a major market and a source of raw material and cheap labor.

25X1

25X1

25X1

In examining the Japanese investment data, it is clear that there is a link between investments in the manufacturing and commerce and service sectors. Japan's service and trade investments in a number of countries established a marketing network for exports as well as a working relationship with local financial institutions. Such a network often served as a forerunner for manufacturing investments, which moved in later. Afterservice investments for manufactured products are also part of this process. Such a pattern can be seen in the consumer electrical appliance and automotive industries, for example.

25X1

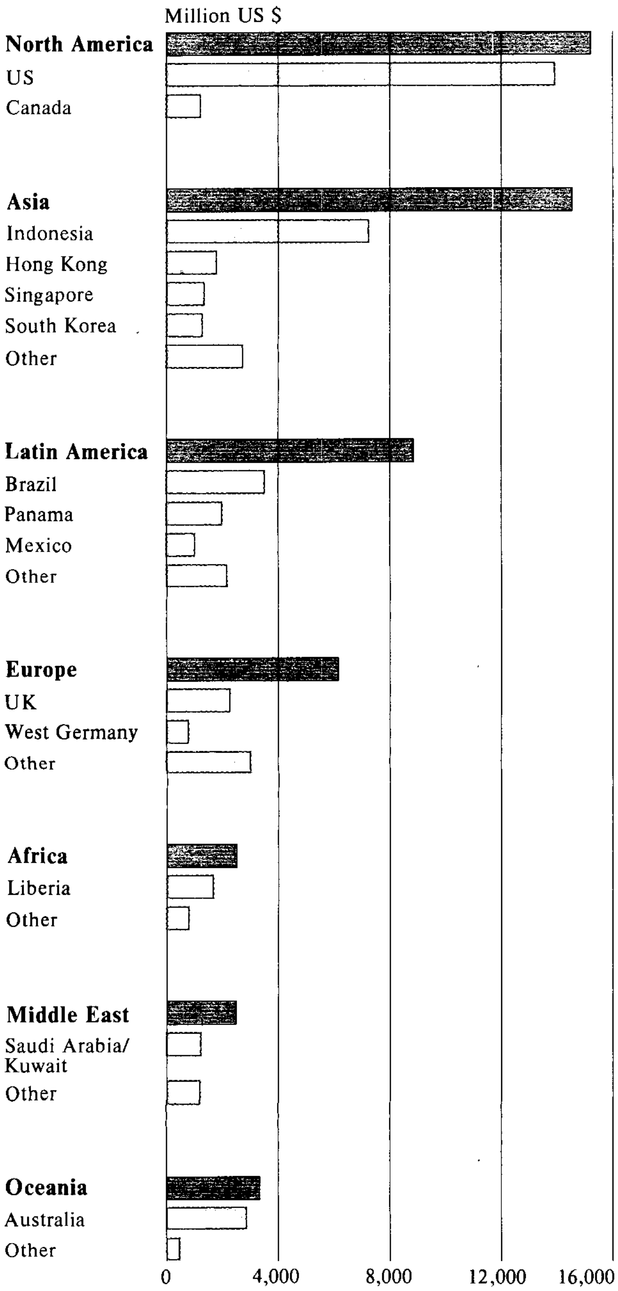
25X1

By the late 1970s changes were also occurring within the manufacturing sector:

- Investments in labor-intensive industries peaked by 1974 and then waned, largely as a result of increased labor costs in developing countries.

25X1

Figure 1
Japan: Cumulative Overseas Investment by Region—FY 1951-81



589982 6-83

25X1

- Investments in such basic capital-intensive industries as chemicals and metals increased rapidly with the escalation of costs of energy and raw material imports, competition from newly industrializing countries, and concern over pollution in Japan.

- By the end of the decade, investments in the machinery industries, particularly the electric machinery and automobile assembly industries, were rising noticeably. 25X1

In FY 1981 new capital investments reached a record $8.9 billion, 90 percent above the FY 1980 level. This surge was marked by significant increases in manufacturing ventures in advanced countries, particularly in the electrical, machinery, and automotive industries, and the completion of several large-scale projects in stable LDCs, such as the development of liquefied natural gas (LNG) in Indonesia. 25X1

According to recently released Ministry of Finance compilations for FY 1982, Japan's direct private investments abroad slowed to $7.7 billion, less than the increase in FY 1981 but a significant improvement over the annual figures for the 1970s' earlier performances (see figure 2). Japanese enterprises stepped up direct investments in industrialized nations while reducing investments in developing nations. New investments in Asia dropped almost 60 percent; in contrast, North America increased 15 percent and Western Europe 10 percent:

- There were no large-scale investments, such as the $1.8 billion LNG project in Indonesia in 1981.

- Yen depreciation of about 10 percent in FY 1982 undoubtedly dampened some investor interest in overseas ventures.

- The general slowdown of the world economy, a deepening domestic recession, and corporate wariness of investing in a growing number of economically or politically unstable developing countries were also factors. 25X1

Sanitized Copy Approved for Release 2011/02/07 : CIA-RDP84S00553R000200170002-8

Table 1
Japan: Overseas Investment Through March 1982 by Region and Industry

Million US $

	North America	Latin America	Asia-Pacific	Europe	Africa	Middle East	**Total**
Manufacturing	**3,409**	**3,034**	**6,120**	**1,042**	**154**	**1,093**	**14,852**
Foodstuffs	312	150	214	44	8	0	**728**
Textiles	207	361	967	151	38	4	**1,728**
Timber and pulp	368	189	266	0	0	0	**823**
Chemicals	283	507	957	119	16	972	**2,854**
Iron and steel, nonferrous metals	395	825	1,630	164	75	52	**3,141**
Machinery	342	275	341	132	0	10	**1,100**
Electrical machinery	992	251	621	173	5	12	**2,054**
Transportation equipment	339	379	536	97	6	4	**1,361**
Other	171	97	588	162	6	39	**1,063**
Nonmanufacturing	**8,886**	**4,317**	**9,998**	**4,226**	**1,863**	**1,260**	**30,550**
Agriculture and forestry	229	150	297	0	7	2	**685**
Fisheries	81	78	120	2	54	1	**336**
Mining	693	1,223	6,277	859	516	39	**9,607**
Construction	156	142	119	31	19	24	**491**
Commerce	4,052	537	865	1,115	3	11	**6,583**
Other	3,675	2,187	2,320	2,219	1,264	1,183	**12,848**

25X1

Corporate Strategies

Although motives vary among individual companies, recent surveys showed that concern about future markets was the primary reason for investing overseas. In the past, Japanese companies had shifted the production of resource, labor, energy, or pollution-intensive processes to developing countries. The newer investments, however, have mainly come from higher technology industries such as automobiles, color televisions, video tape recorders, video disks, plain paper copiers, facsimile machines, personal computers, and word processors. Although labor cost remains a factor, it is not sufficient by itself to lead a company to move production overseas.

Japan's auto industry is a clear example of the trend toward overseas investment to assure market access (see inset page 5). With the domestic market for automobiles nearing saturation and shipments abroad being limited by restraint agreements, Japanese automakers began to expand their assembly operations to the United States and other developed countries. In the early 1970s many had already set up manufacturing plants in Southeast Asia because of local content requirements and other restrictions on exports.

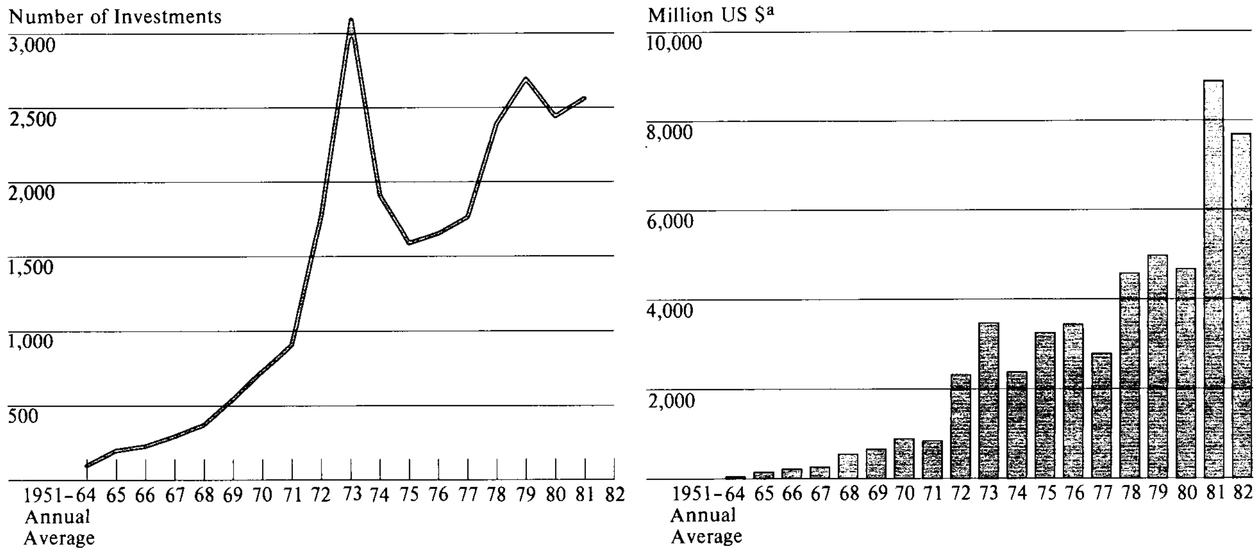
25X1

Japanese manufacturers are usually reluctant to invest in overseas production facilities if they doubt that profits or quality control can be maintained. For example, despite being wooed by the British Government, Nissan has been reluctant to set up an assembly plant in Britain for fear that Parliament might pass pending local content legislation requiring up to 80 percent of locally made parts in vehicles, according to a leading economic journal. Nissan also reportedly is concerned that the vehicles produced at such a plant may still be considered a foreign import by other EC countries and thus subject to high tariff and duties if exported to other European countries.

25X1

25X1

Figure 2
Japan: Growth of Overseas Investment, 1951-81



[a] Approvals.

25X1

589983 6-83

Honda Motors, one example of a Japanese manufacturer expanding quickly into the global market, has established a network of offshore production facilities operating in 30 countries, including its new auto plant in Ohio. Honda was able to move rapidly into offshore auto assembling because it had earlier established an offshore base to produce and market motorcycles. In many cases, it was able to add to existing facilities to produce cars. Honda now has 43 offshore plants, produces automobiles in six countries, motorcycles in 24 countries, and parts in five countries. It also has licensing arrangements with local companies in the United Kingdom to produce cars and in France and China to produce motorcycles. The overseas ventures account for 20 percent of Honda's current profits.

A number of leading Japanese companies have already begun to form joint ventures with US or West European firms to develop and produce advanced-technology products. Sumitomo, for example, plans to open a plant in the United States to manufacture fiber-optic cables in a joint venture with Corning Glass. Other joint ventures currently operating or in the planning stages include such products as carbon fibers, oil drilling equipment, nuclear generating and radiological equipment, jet engines and planes, and LNG tankers. 25X1

Such newly industrializing countries as South Korea, Hong Kong, and Taiwan are now requesting foreign investments in knowledge-intensive industries. Fanuc, the leading Japanese robot maker, recently formed a joint venture with the Kolon Group in South Korea to assemble industrial robots in that country in 1983. Similarly, Matsushita Electric recently announced plans to assemble industrial robots in Singapore, and Mabuchi has established wholly owned subsidiaries in Hong Kong and a joint venture in Taiwan to manufacture minimotors for overseas sales. 25X1 25X1

Once Japanese manufacturers make a major investment to produce offshore, they often seek to attract their equipment suppliers in the home market to

The Nissan Story

Nissan is involved in auto and truck production facilities in eight countries—the United States, Mexico, Peru, Australia, Spain, Italy, Thailand, and the Philippines. In 15 other countries, Nissan's cars are assembled under license. Nissan now owns 55 percent of Motor Iberica S. A., Spain's leading manufacturer of commercial and farm vehicles. With a total work force of 8,000, the company will soon begin to assemble four-wheel drive and other vehicles for domestic and export sales. Nissan hopes to satisfy demand in Spain and to gain access to the lucrative EC auto market. Spain is scheduled to join the EC later this decade. Spain currently does not permit any imports of Japanese motor vehicles.

In Italy, which imports only 2,000 Japanese cars per year, Nissan has established a 50-50 joint venture with Alfa Romeo to produce small-sized passenger cars starting this year, again with an eye to the broader European market. In Australia, Nissan's assembly plant supplies the domestic market with finished automobiles but eventually may export to the entire Oceania region. More than 85 percent of the parts for Australian-made Nissan automobiles are mandated by law to be procured from local parts manufacturers. The amount drops to 70 percent if the cars are to be exported. 25X1

In Peru, Nissan holds a 56-percent share in a joint venture, Nissan Motor del Peru S. A., which produces 1,000 cars a month and employs 700 workers. Nissan has been the top auto seller in Peru since 1978. In the Philippines, Nissan and Marubeni Corporation each had to take a 15-percent share in Pilipinas Nissan, Incorporated (PNI) with the rest owned by a government-licensed local partner in order to obtain manufacturing rights in that country. 25X1 *The Philippine Government prohibits passenger car production by nonlicensed companies.* 25X1

The most recent addition to Nissan's overseas production base is a truck plant in Smyrna, Tennessee. Nissan's investment of $660 million in the project is the largest manufacturing investment ever made in the United States by a Japanese company 25X1

follow. Apparently concerned about the quality and availability of automobile parts, for instance, Nissan convinced some of its parts suppliers, such as Bridgestone Tire, to set up plants in Tennessee. In ASEAN countries, Japanese automakers have brought in some of their component suppliers in response to local content requirements.[2]

Major trading houses also have played a major role in increasing Japan's overseas manufacturing presence, accounting for more than 40 percent of overseas investments in the 1960s and early 1970s. Manufacturing investments by major trading houses tend to be mainly in the areas of textiles, chemicals, iron, and steel. The trading houses also have played a role in large-scale resource and energy-related industrial projects. In the 1980s the trading companies have continued to focus on investments associated with the relocation of Japan's basic industries such as aluminum smelting, petrochemicals, and pulp and paper as well as energy-related industries. Such investments usually involve much greater risks than small-scale 25X1 manufacturing facilities. Japanese trading companies are more willing than other Japanese firms to take these risks because of their vast network of trading offices and commercial intelligence. For example, Mitsui has established a soft drink bottle factory in Nigeria, even though the main raw material—caustic soda—is expensive and difficult to transport. Mitsui found a source in Kenya and pioneered shipments of the commodity from Kenya to Nigeria around the Cape. 25X1 25X1 25X1

[2] The Association of Southeast Asian Nations comprise Thailand, Indonesia, the Philippines, Malaysia, and Singapore.

Table 2
Top 20 Japanese Firms in Overseas Investment as of March 1982

Million US $

Ranking	Name of Firms	Outstanding Balance of Investment [a]
1	Mitsui and Company	922.9
2	Mitsubishi Corporation	879.5
3	Iran Chemical Development	792.0
4	C. Itoh and Company	518.5
5	Nissan Motor	441.8
6	Marubeni Corporation	439.0
7	Sumitomo Corporation	390.0
8	Sanko Steamship	318.5
9	Nippon Asahan Aluminum	312.4
10	Matsushita Electric Industry	303.6
11	Toshiba Corporation	290.8
12	Japan Leasing	283.5
13	Kawasaki Steel	266.3
14	Honda Motor	258.6
15	Toyo Menka	237.3
16	Sony	222.9
17	Nissho Iwai Corporation	221.3
18	Kawasaki Heavy Industries	217.3
19	Toray Industries	215.7
20	Fujitsu	205.6

[a] Calculated based on the 1982 average exchange rate of 249 yen to the dollar. Figures are based on company reports of overseas investments and not official data.

In recent years, five trading firms led by Mitsui began to invest heavily in US agriculture, purchasing grain elevators and other facilities in the Gulf coast, west coast, and Great Plains states to ensure Japan a steady and cheap supply of soybeans, feedgrain, wheat, and other grains. Moreover, grain storage in the United States is less expensive than in Japan, and the companies also were interested in exporting grain to third countries. The trading companies, however, have suffered substantial losses from this venture because of slumping prices in the United States. 25X1

The Internationalization of Small Businesses

Another recent trend has been the willingness of small- and medium-sized Japanese businesses to invest overseas. According to the Ministry of International Trade and Industry (MITI), the pace of such investments began to pick up in the late 1970s. Over the three-year period, 1978-80, small- and medium-sized firms made up 51 percent of the total number of new overseas investments. The percentage in 1976 was only 33 percent. In 1981 small- and medium-sized businesses accounted for two-thirds of the investments in North America. 25X1

Most of the overseas investments by smaller firms are in trade and service activities. Only about a fourth are in manufacturing, mainly electrical machinery and foodstuffs, but the pace of new manufacturing investments is increasing. This could reflect the slowdown in the rate of growth in Japan's domestic economy, which may be pushing these enterprises to seek business opportunities overseas. In addition, Japan's large firms have increasingly urged smaller companies to follow overseas as subcontractors. 25X1

Japanese small- and medium-sized enterprises formerly aimed their overseas manufacturing investments primarily at developing countries in order to take advantage of lower overseas labor costs, usually in labor-intensive light industries. Some were tied to investments of Japan's large trading houses. Recently, however, smaller companies have been investing in production facilities in advanced countries. These outlays are higher on the technology scale and are less likely to be tied to trading company operations. Some firms are manufacturers of software and hardware, others use computer technologies to churn out products such as component parts for Japanese automobile or electronic appliance makers, or develop new products including lasers, plastics, and special machinery for domestic and overseas marketing. 25X1

25X1

Japanese Direct Investments in the United States

As a share of total Japanese outlays, investments in the United States have been accelerating and now account for 26 percent of Japan's total global direct investments. The cumulative total reached $13.9 billion in FY 1982. Indonesia is second on the list with 15 percent. Since 1979 Japan's investments in the United States have doubled and continue to rise rapidly, according to the US Department of Commerce. Japan accounted for 8 percent of foreign direct investment in the United States in 1981, up 2 percent over 1980. The share in 1973 was only 1 percent. [redacted] 25X1

Table 3
Japan: Direct Investment in the United States [a]

Year [b]	Total Overseas Investment *(Million US $)*	Investment in the United States *(Million US $)*	US Share of Total Investment *(Percent)*
1970	904	94	10.4
1971	858	216	25.2
1972	2,338	356	15.2
1973	3,494	801	22.9
1974	2,395	498	20.8
1975	3,280	846	25.8
1976	3,462	663	19.2
1977	2,806	686	24.4
1978	4,598	1,283	27.9
1979	4,995	1,345	26.9
1980	4,693	1,484	31.6
1981	8,906	2,329	26.2
1982	7,703	2,709	35.2

[a] Approvals.
[b] Fiscal year.

[redacted] 25X1

A recent survey by the Japanese Government–funded Japan Economic Research Institute disclosed that manufacturing investments accounted for only 18 percent of all Japanese direct investment cases in the United States. In contrast, 57 percent of the investments were in commerce such as sales and trading offices. However, more than a third of the manufacturing investment cases had entered the United States since January 1980 and almost two-thirds since the late 1970s. Recent investments have included electrical machinery (especially color TVs and home appliances), electronics equipment, communications equipment, semiconductors, machine tools, motorcycles, pharmaceuticals, foodstuffs, chemicals, iron and steel, nonferrous metals, and, most recently, automobiles. Japanese TV makers are setting up plants or using existing plants to make video tape recorders and video disks. [redacted]

Much of the recent flurry of Japanese investment activity in the United States has been in high-technology products where demand has soared so rapidly that it cannot be met solely by Japanese exports. Many investments, such as those in semiconductor manufacturing, reflect corporate desire to avoid future trade frictions by using local production. Cost savings and fierce competition in the industry have also influenced investment decisions, according to official surveys. [redacted]

In 1981, for example, four leading manufacturers of semiconductors—NEC, Hitachi, Toshiba, and Fujitsu—all began production in the United States. NEC also plans to open a new large-scale semiconductor factory in California, which will eventually employ 600 workers. It is also opening a factory near Boston to manufacture office computers. Kyocera operates four production facilities in the United States to produce ceramic packaging for integrated circuits and other electronic parts. The main plant in San Diego employs over 1,200 workers. Although some investments through company takeover or joint venture are made in order to obtain advanced technology, most appear to be in products where Japanese technology is equal or superior to US competitors. 25X1

[redacted] 25X1

The current investment boom, part of a general world trend to invest in the United States, was set off in the late 1970s during a period when the dollar was weak against most foreign currencies, making imports more expensive in the United States. Since 1978, according to the US Department of Commerce, the United States has received more investment funds—particularly from Japan and the EC—than at any time since 25X1 the 19th-century railway boom. For many foreign firms, it became more profitable to produce locally or to buy up local firms than to export to the United States. Other investors were attracted to the United States because of the availability of cheaper raw materials. As many as 14 plastic product companies, for example, began production in the United States because of low-priced US petroleum feedstocks. A number of Japanese firms bought sawmills and paper plants to take advantage of the low cost of local raw materials. [redacted]

One noteworthy aspect of Japanese direct manufacturing investments in the United States is that Japanese firms, according to official and private surveys, prefer to establish new plants rather than buy out existing production facilities. By building new facilities the companies have created more jobs in the local areas. Japanese manufacturing affiliates in the United States also tend not to be joint ventures, but wholly owned subsidiaries. European corporations have usually bought out existing US companies. [redacted]

Historically, most Japanese manufacturing investment in the United States has been small scale, employing less than 300 persons per production facility. About 60,000 persons are now employed at Japanese plants in the United States. The average size of investments has been increasing, however. Large-scale auto, truck, and other assembly plants now in operation should push the average employment up significantly since such plants employ between 1,000 and 3,000 workers. [redacted]

Manufacturing Investments in Western Europe

Japanese direct investments in Western Europe totaled $6.2 billion in FY 1982. The bulk has gone to the United Kingdom, which is the fifth-largest recipient of Japan's direct investments, holding $2.1 billion as of FY 1981. Roughly 20 percent of the total Japanese outlays in Western Europe is in manufacturing. [redacted]

Japanese direct investments in Western Europe lag far behind those in the United States mainly because Japanese firms have found the investment climate less welcome. Recently, however, many European countries have begun to court Japanese firms. New investments were up 38 percent—about $800 million—in FY 1981. Nonetheless, some countries—particularly France, Greece, and Italy—remain basically hostile toward Japanese companies despite some recent joint ventures in high-technology products. [redacted] 25X1

Japanese firms have ignored positive incentives, however, in some countries. In the case of Northern Ireland, Ulster officials have tried to woo Japanese 25X1 firms by promising assistance, touting the benefits of low labor costs and highlighting the education level of the labor force. Japanese firms, fearing terrorist activity, have not responded enthusiastically. They have not been afraid, however, to set up plants in the Republic of Ireland, which they view as safer. [redacted] 25X1

Western Europe has a long tradition of limiting Japanese exports through tariffs, voluntary restraints, harassment, and local content requirements. Japanese products subjected to such discrimination include 25X1 textiles, electrical equipment, automobiles, motorcycles, china, cutlery, bearings, color televisions, and quartz watches. Much of the planned or current manufacturing investments are joint ventures by producers of these goods with local partners designed to get around trade barriers. [redacted] 25X1

ASEAN: Changing Pattern of Japanese Investments

25X1

Japanese academics who have studied long-term investment trends conclude that Japanese businessmen have long regarded ASEAN as relatively safe for investment capital, although Thailand, because of its precarious geopolitical position, and the Philippines, because of its economic woes, are considered higher risks than the other ASEAN countries. According to surveys of Japanese businesses, the most common reasons why Japanese investors favored ASEAN were market expansion for their products, cheap labor, and government policies in ASEAN countries designed to

25X1

Table 4
Japan: Investment in the Manufacturing Sector of ASEAN Countries

Million US $ (except as noted)

	ASEAN		World		ASEAN's Share of Japan's Global Investments	
	End of CY 1976	End of CY 1980	End of CY 1976	End of CY 1980	End of CY 1976	End of CY 1980
Foodstuffs	85	118 (3.7 percent)	314	587 (4.7 percent)	27.1	20.1
Textiles	454	608 (19.0 percent)	1,128	1,637 (13.0 percent)	40.2	37.1
Lumber/pulp	98	125 (3.9 percent)	578	758 (6.0 percent)	17.0	16.5
Chemicals	109	417 (13.0 percent)	1,044	2,626 (20.9 percent)	10.4	15.9
Iron/nonferrous metals	182	913 (28.5 percent)	953	2,619 (20.8 percent)	19.1	34.9
General machinery	49	163 (5.1 percent)	452	894 (7.1 percent)	10.8	18.2
Electrical machinery	91	243 (7.6 percent)	687	1,579 (12.6 percent)	13.2	15.4
Transport machinery	118	239 (7.5 percent)	453	979 (7.8 percent)	26.0	24.4
Other	185	371 (11.6 percent)	460	894 (7.1 percent)	40.2	41.5
Total	**1,372**	**3,198 (100.0)**	**6,065**	**12,573 (100.0)**	**22.6**	**25.4**

[redacted] 25X1

attract new foreign investments. Other reasons included local restrictions on imports of certain finished products, such as automobiles, or to compete with other Japanese companies in ASEAN. [redacted]

Japan's cumulative direct investments in ASEAN reached nearly $10 billion in early 1982. About 70 percent of that is concentrated in Indonesia, mainly in several large-scale resource development projects. Japan is Indonesia's largest foreign investor, supplying more than 37 percent. Based on preliminary reports for 1982, this share is edging higher; 40 percent of new foreign investments approved by the Indonesian Government last year were Japanese. [redacted]

For the region as a whole, however, the pace of Japanese outlays has slowed somewhat, in part because Japanese firms are less involved in labor-intensive industries such as textiles (see table 4). Most new investments in the manufacturing sector have been into more advanced industries such as electrical machinery and machinery (Singapore) and into heavy industries such as metals fabrication (Indonesia). [redacted]

Japanese investors in ASEAN usually set up a joint venture with local partners and are minority shareholders, reflecting in part host-country restrictions on equity participation. In the past, Japanese investors 25X1 have also favored group investments, often involving a Japanese trading company, to share the risk. Investments in newer types of industries, however, usually do not involve trading houses, probably reflecting the trading firms' limited knowledge of high-technology sectors. [redacted] 25X1

Profitability of Overseas Investments

Japanese firms have generally found overseas investments to be profitable: 25X1

- According to a MITI survey in 1981, 70 percent of overseas affiliates were making profits and revenues from overseas enterprises accounted for 5.4 percent of current profits of the parent companies.

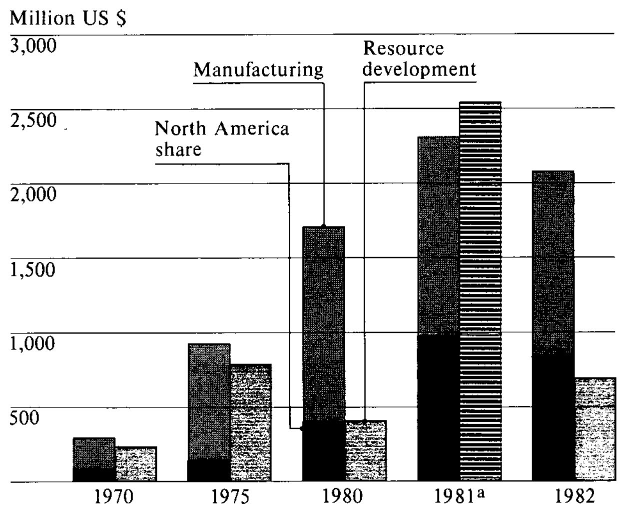
25X1

- The Ministry of Finance reports that the net return on direct investments received by Japanese companies in FY 1982 reached a record $1.45 billion, despite the world recession.

- Automobile and electronic companies have led the list of industries with good earnings in recent years. For example, Nissan's overseas subsidiaries in West Germany, Mexico, Canada, and Peru have recently begun paying dividends to the parent company; its nonmanufacturing subsidiary in the United States has been paying dividends for years. Matsushita Electric last year announced a 15-percent increase in its dividend revenues from abroad based on fiscal year 1981 performance. [redacted] 25X1

These rising revenues from abroad also are shifting Japan's international balance-of-payment position. Repatriated profits helped trim Japan's traditionally large deficit on the service account from 13.6 billion to 9.9 billion in 1982. In certain months of 1982, remittances from abroad in the form of dividends accounted for more than half of Japan's current account surplus. [redacted]

Figure 3
Japan: Overseas Investment in Manufacturing and Resource Development



[a] The large jump in resource development in 1981 is the result of a one-time, large-scale LNG project in Indonesia, worth almost $2 billion. 25X1

[redacted] 25X1

589984 6-83

The Role of Government

The Japanese Government has played an active role both publicly and behind the scenes in encouraging investment. In the 1960s and 1970s Tokyo fostered outlays in resource development to ensure access to raw materials and in manufacturing in low-wage countries to help Japanese companies maintain their international competitiveness. Recently, however, the emphasis has switched to encouraging manufacturing investments in advanced countries to counter rising criticism of Japan's trade policies and to cope with protectionist measures (see figure 3). The government is encouraging foreign direct investment inside Japan for similar reasons. [redacted]

Under the foreign exchange control system, overseas direct investment by Japanese companies is unrestricted except in fishing, banking, securities, leather, textiles, weapons, and narcotics industries. In restricted sectors, specific approval from Tokyo is required. The procedure in other areas has been greatly simplified over the past few years; now Tokyo requires only prior notice to the Finance Ministry with a 20-day waiting period. [redacted] 25X1

Tokyo uses a number of programs, incentives, and measures to encourage overseas investment. MITI provides risk insurance against losses caused by nationalization, war, or internal uprising in host countries. In 1980 MITI's insurance underwrote about 10 percent of the total value of direct investments overseas. This small number reflects the tendency of Japanese businesses to choose investments in stable countries where such insurance would not be necessary. Some companies, however, have found the insurance handy. Bridgestone Tire Company had its 25X1

$12.9 million investment in Iran nationalized in late 1979. Unable to recover its right to manage the plant or its investment, Bridgestone finally decided to pull out of Iran in August 1982 and filed an insurance claim with MITI. Mitsui wanted to pull out of its petrochemical project in Iran after it was halted by the Iran-Iraq war, but MITI discouraged disinvestment because of the enormous amount of risk insurance it would have to pay.

More investors may turn to this fund because of mounting concern over defaults and unstable conditions in many LDCs. The Japanese press also reports that some businessmen want MITI to expand its risk insurance program. To help cope with this problem, the Ministry of Finance has also created a new office to examine host-country financial risks and make its findings available to financial institutions.

Official financial institutions provide only a small amount of the cash needed by Japanese investors for overseas ventures. In 1979, for example, about 10 percent of overseas investments were funded by loans from official financial institutions, a decline from the 29.5-percent peak reached in 1975. Over half came from parent companies' own resources, while less than a fourth relied on loans from commercial establishments.

Government institutions, nonetheless, have the ability to aim their limited funds at selected countries or types of investments, which are of immediate policy interest to the Japanese Government. The Japan Export-Import Bank, which takes its guidance from the Ministry of Finance, has been charged with implementing the government's policy to ease trade frictions with advanced countries through industrial cooperation. The Bank's specific role is to provide financial assistance and extensive consultative services for Japanese firms planning manufacturing investments in Western Europe or the United States. Almost a fourth of the Bank's total lending authority for FY 1983 has been earmarked for this purpose—about triple the authorized level in the FY 1982 budget. The most visible example of the Bank's new role is its backing of Nissan's new truck plant in Tennessee, where it will finance 60 percent of the $500 million Nissan needs. The remaining 40 percent will come from a nine-bank consortium.

The government established an overseas investment system in 1981 to help small- and medium-sized firms invest overseas. The program, administered by the quasi-official Japan Small Business Corporation, provides technical information and advice on joint ventures, contracts, licensing operations, and selection of business partners. It also advises businesses on plant and office construction, employment practices, and financial practices in host countries. Surveys evaluating country risks and prospective partners are also conducted.

25X1

25X1

Often working closely with MITI and other government agencies, private economic organizations in Japan such as the Keidanren or Keizaidoyukai, whose memberships include Japan's most powerful corporations, actively promote overseas investment among their member firms. The Keizaidoyukai, for example, has set up special facilities to promote investment in ASEAN. The Keidanren organizes and leads investment missions abroad.

25X1

25X1

The organizations also offer a whole range of informational services to prospective overseas investors, supplementing those offered by financial and governmental institutions. Keidanren has long had an International Investment and Technical Exchange Committee and in 1982 established a special committee, chaired by Sony board chairman Akio Morita, to act as a clearinghouse for foreign governments that request direct investments by Japanese firms. In the past, foreign governments had to seek out firms directly.

25X1

25X1

Impact on Japan

Thus far the increase in offshore production has not hurt Japan's domestic work force, primarily because there have been other industries to take up any employment slack and because parent companies continue to manufacture and ship component supplies to overseas assembly plants. With the increased pace of such shifts to offshore production and the increase in unemployment, some in Japan are becoming increasingly concerned.

25X1

25X1

Recently, MITI commissioned a study to look into the possibility of unemployment resulting from the rapid expansion of overseas manufacturing investment. The study, by a private research organization, concluded that the domestic impact would probably be neutral as long as foreign manufacturing facilities use components produced in Japan. Private industry and labor in Japan are not as optimistic. In a Ministry of Labor study in 1982, some corporate officials and labor unions cited the Nissan plant in Tennessee as an example of an investment that could lead to unemployment at the truck plant in Kyushu, which has produced almost solely for the US market. [redacted]

Conclusions and Prognosis

[redacted] if current trends continue, Japan's overseas direct investments will reach $100 billion or about 10 percent of the world's total stock by 1990. [redacted] about $33 billion will be located in the United States, about half of that in the manufacturing sector. [redacted]

We believe these projections are reasonable. Faced with changing international economic conditions and the need to maintain access to overseas markets, Japanese export industries should continue to shift part of their production base offshore and Japanese manufacturers should lead the way in an attempt to ease trade frictions. We also believe the Japanese Government will continue to encourage manufacturing investments in advanced countries through financial assistance and other incentive programs in an effort to deal with protectionist sentiment in those market countries. [redacted]

Japanese direct investments in the United States during the 1980s should remain strong. Reflecting both the fear of new trade barriers and the large stock of Japanese cars already in the United States, transport machinery manufacturers and their parts suppliers should continue to open new production lines and expand existing lines. In terms of numbers of investments, however, the electronics industry and other Japanese high-technology industries could lead the list as Japanese firms continue to seek links to US companies as well as guarantee access to the US market. [redacted] 25X1

For US firms, joint ventures with Japanese firms will be both a challenge and an opportunity. The US company will have to decide how much technology to share with its partner. [redacted] 25X1
US firms now are more worried about the impact of sharing technology with a potential competitor. On the other hand, joint ventures could also give US firms access to Japanese technology and managerial expertise. Industry press, for example, suggests that GM will benefit in such a way from its joint venture with Toyota to produce cars in California. [redacted] 25X1 25X1

Based on survey data, we believe Japanese firms will continue to favor the US Sunbelt states. Many of these states have made special efforts to attract Japanese manufacturing investments. [redacted] 25X1 25X1 25X1

Under the current capital-to-labor ratio, $1 billion in new Japanese investment in the United States would create 5,000 new jobs. This, however, probably sharply understates the impact because the new investment is likely to be in the manufacturing sector, which is more labor intensive. Official Japanese surveys already show that the average number of employees per overseas firm is increasing. [redacted] 25X1 25X1 25X1 25X1

Japan's direct investments in stable LDCs will continue to emphasize basic materials industries such as steel, aluminum, and petrochemicals, but the pace of new investments should be slower than in the previous decade because of a glut of those products in the world market. We believe ASEAN will continue to be the primary beneficiary of Japan's direct investments in developing countries in the 1980s, including Japan's declining smokestack industries such as petrochemicals, paper and pulp, and aluminum. Finally, Japanese industrialists should continue to respond positively but cautiously to ASEAN requests for advanced technology through technology transfers, licensing, and the introduction of knowledge-intensive 25X1 industries. Japan has already agreed to establish technology transfer centers in each ASEAN capital to provide technical training based on what is mutually judged to be appropriate to the needs of the country. [redacted] 25X1

Japan's drive to secure stable sources of energy and other critical resources will slow in the 1980s because of slower domestic growth. Moreover, Tokyo is limiting the official financial backing for such projects. Nonetheless, Tokyo remains sensitive to Washington's interests in joint ventures and will not rule out involvement in coal, oil, or gas projects in the United States even though Japanese industry complains about high costs. [redacted] 25X1